

## STAFF PAPER

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**Rate-regulated Activities Consultative Group**

Project	Rate Regulation		
Paper topic	Scope Issues: Prices that bind customers		
CONTACT(S)	Jane Pike	<a href="mailto:jpike@ifrs.org">jpike@ifrs.org</a>	+44 (0)20 7246 6925

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**Introduction**

1. The scope of the proposals in Exposure Draft Rate-regulated Activities, published in July 2009 (the 2009 ED) was restricted to a particular type of rate regulation; “cost-of-service” regulation (paragraph 3 of the 2009 ED):

“3 An entity shall apply this [draft] IFRS to its operating activities that meet the following criteria:

(a) an authorised body (the regulator) establishes the price the entity must charge its customers for the goods or services the entity provides, and that price binds the customers; and

(b) the . . . . .”

2. The Exposure Draft *Regulatory Deferral Accounts*, published in April 2013 (the 2013 ED), contained the same scope criterion. Some respondents to the 2009 ED were concerned that this criterion places too much weight on the price set by the regulator. They questioned whether entities that have some flexibility in pricing would be captured within the scope.

**Pricing flexibility**

3. The introduction to the Request for Information *Rate Regulation*, published in March 2013 (the RFI), defined rate regulation as “the mechanism by which a rate

regulator imposes control over the setting of prices that can be charged to customers for services or products”.

4. As noted in the summary of responses to that RFI (agenda paper 4 for this meeting), the price- or rate-setting mechanisms used by rate regulators vary widely. As well as the wide variety of formulas used to identify the price to be charged, the way that suppliers have to apply the price also varies. Examples include:

- (a) A fixed price per unit that is charged to all customers in the whole customer base, irrespective of volume;
- (b) The whole customer base is divided into different groups of customers (for example, wholesale customers and retail customers) and a fixed price per unit is designated for each group, with that price charged to each customer within the group;
- (c) The regulator may set a maximum price, but the supplier can provide the regulated goods or services at a discount to that price – either to groups of customers or to individual customers;
- (d) The price might be set as a range of permitted prices (with a ceiling and a floor), instead of a single point price;
- (e) The price might be set on a per unit basis according to one of the mechanisms above, but the supplier’s overall revenue is capped at a maximum amount (although the supplier may also be able to earn overall revenue subject to a floor). In such cases, the supplier may have some flexibility to adjust prices throughout the rate-regulatory period or any over- or under-recovery may be tracked and only adjusted through future price adjustments within the formal rate-regulatory adjustment.

5. In some cases, a regulator may impose a cap on prices to be charged, without reference to the costs incurred by the suppliers of the goods or services that are subject to price cap. For example, in Europe, there is a ‘blanket’ cap placed on mobile telephone ‘roaming’ charges across several countries; and in some jurisdictions there is a cap on the price that can be charged for processing credit card transactions. Entities may charge lower prices than the maximum level of the capped price.

6. The wording of the RFI is intentionally designed to be broader than the scope of both the 2009 ED and the 2013 ED because we did not want to restrict our investigation of pricing structures to only those where a single fixed price was set by the rate regulator. It can be seen by the summary of responses that some entities do consider themselves to be rate regulated even when they are allowed some flexibility in pricing.

## Questions for the Consultative Group

### Defining the scope

1. Do you agree that rate regulation is a “mechanism by which a rate regulator imposes control over the setting of prices that can be charged to customers for services or products”, even when that control permits entities to have some flexibility in the actual price charged?
2. Are there any types of pricing control that you think should be excluded from the scope of the planned Rate Regulation Discussion Paper? If so, please explain why.